

Decision **DRAFT DECISION OF ALJ WONG** (Mailed 2/18/2005)**BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA**

In the Matter of the Application of Southern California Gas Company (U 904 G) Regarding Year 10 (2003-2004) of Its Gas Cost Incentive Mechanism.

Application 04-06-025
(Filed June 15, 2004)

**OPINION REGARDING YEAR 10 OF THE GAS
COST INCENTIVE MECHANISM****Summary**

Today's decision addresses the Year 10 Gas Cost Incentive Mechanism (GCIM) application filed by Southern California Gas Company (SoCalGas) on June 15, 2004.

The decision finds that SoCalGas reasonably managed its gas acquisitions and operations in Year 10 within the context of the GCIM that existed at the time, and that the calculation and amount of the shareholder award is correct. Pursuant to the GCIM modifications adopted in Decision (D.) 02-06-023, SoCalGas is awarded a shareholder award of \$2,364,577 for Year 10.¹

Due to the ongoing activities in the Order Instituting Investigation (I.) 02-11-040, the finding of reasonable management shall not prejudice what we may find or conclude in I.02-11-040, and the SoCalGas shareholder award shall be subject to refund or adjustment as may be determined by us in I.02-11-040.

¹ SoCalGas has rounded this amount and refers to this amount as \$2.4 million.

Procedural and Factual Background

The GCIM is a Commission-authorized ratemaking mechanism that SoCalGas uses to purchase natural gas on behalf of its core customers. The GCIM replaced the reasonableness reviews of SoCalGas' procurement activities. The GCIM establishes a benchmark against which to measure the price that SoCalGas pays for gas. This provides an incentive for SoCalGas to purchase gas at or below the benchmark. Savings below the tolerance band are shared with ratepayers and SoCalGas' shareholders according to the sharing band adopted in D.02-06-023.

SoCalGas was first authorized to use the GCIM in D.94-03-076 [53 CPUC2d 663]. The GCIM was modified in D.02-06-023, and SoCalGas was authorized to continue the use of the GCIM on an annual basis until modified or terminated by the Commission.

On June 15, 2004, SoCalGas filed its Year 10 GCIM application. SoCalGas' application describes the results of operations under the GCIM structure for its gas acquisition activities for Year 10, the period from April 1, 2003 through March 31, 2004.

Responses to SoCalGas' application were filed by the Office of Ratepayer Advocates (ORA) and The Utility Reform Network (TURN) on July 19, 2004 and July 23, 2004, respectively. Southern California Edison Company (SCE) filed a protest to the application on July 23, 2004. On August 2, 2004, SoCalGas filed a reply to SCE's protest and to TURN's response.

On October 15, 2004, ORA served its Monitoring and Evaluation Report on the Year 10 GCIM.

A ruling of the assigned administrative law judge (ALJ) was issued on December 8, 2004 proposing a procedure to resolve the issues in this proceeding.

The ruling provided an opportunity for parties to file an objection to the proposed procedure. No one filed any objection.

On January 12, 2005, the assigned Commissioner issued a scoping memo and ruling (scoping memo). Since no one raised any issues requiring a hearing, the scoping memo concluded that no evidentiary hearing was needed in this proceeding unless a decision issues in I.02-11-040 which determines that the GCIM that SoCalGas was operating under in Year 10 should be modified or eliminated. The scoping memo also stated that following the issuance of the scoping memo a draft decision on SoCalGas' Year 10 application would be prepared and issued for comment.

Positions of Parties

A. SoCal Gas

The Year 10 GCIM application of SoCalGas reports on the results of its gas supply and storage operations for the period April 1, 2003 through March 31, 2004. In accordance with D.02-06-023, SoCalGas requests that the Commission approve a shareholder award of \$2.4 million for its Year 10 performance under the GCIM.

SoCalGas' Annual Report on the GCIM for Year 10, which was attached to SoCalGas' application, notes that "SoCalGas' core customers continued to receive reliable natural gas supplies at below-market cost in Year 10," and that "ratepayers have realized the benefit of gas purchases below the GCIM benchmark ... in nine of the past 10 years." (Application (A.) 04-06-025 Application, Attachment A, p. 1.)

In Year 10, SoCalGas acquired gas at a total savings of \$27,028,710 below the benchmark. Pursuant to the GCIM revisions adopted in D.02-06-023,

of this total savings, \$24.6 million is the ratepayers' share, and \$2.4 million is the shareholders' share.

B. SCE

SCE's protest to SoCalGas' application states that in the prior GCIM proceedings, SCE has asserted that the GCIM "creates perverse incentives, harms noncore customers, and has a detrimental impact on the California energy markets." (SCE Protest, p. 2.) SCE also contends that the ongoing Commission investigation (I.02-11-040) into the cause of the natural gas border price spikes from March 2000 through May 2001 may result in the modification or elimination of the GCIM structure. If the GCIM is modified or eliminated, SCE asserts that this will have a direct bearing on whether SoCalGas' award for Year 10 is appropriate. SCE recommends that any shareholder award should be made subject to refund or adjustment, as was done for the Years Seven, Eight, and Nine applications. (*See* D.03-08-065, D.03-08-064, and D.04-02-060.)

C. ORA

ORA's Monitoring and Evaluation Report for Year 10 was served on October 15, 2004. The report states that ORA conducted a comprehensive audit of SoCalGas' GCIM Year 10 results. This audit included a review of SoCalGas' recorded Purchased Gas Account (PGA) costs, an analysis and verification of the GCIM calculations, and an evaluation of the manner in which the program operated under during the period. The report also states that ORA verified that the current sharing mechanism resulted in a "total savings of \$27.0 million to be split between a ratepayer benefit of \$24.6 million and a shareholder reward of \$2.4 million." (ORA Monitoring and Evaluation Report, October 15, 2004, p. 1-1.) ORA's report also states that "the SoCalGas GCIM operation in Year 10 was

prudent and reasonable and provided benefits to both core customers and the utility.” (*Id.*, pp. 1-12.)

Based on the results of ORA’s audit, ORA recommends that SoCalGas be authorized to recover a shareholder award of \$2,364,577, and that the GCIM be continued.

D. TURN

TURN states that it was a signatory to the settlement agreement that was adopted in D.02-06-023. That decision amended the GCIM, and as part of the settlement agreement, SoCalGas committed to consult with ORA and TURN for interstate capacity commitments longer than two years. In Rulemaking (R.) 04-01-025, TURN recommended that a consultation process for interstate capacity commitments be adopted. D.04-09-022 adopted an interstate pipeline and storage capacity contract consultation process with ORA, TURN and the Commission’s Energy Division.

TURN’s response states that it intends to participate in the review of future commitments for core interstate pipeline capacity. TURN believes that its participation in the consultation process is relevant to SoCalGas’ performance under the GCIM, and requests that any potential intervenor compensation for its participation in this process be considered in the GCIM.

SoCalGas’ reply states that it “has worked closely with TURN in the preparation of SoCalGas’ interstate capacity commitment proposals in R.04-01-025, and we acknowledge TURN’ vital role in the future execution of these proposals.” (SoCalGas Reply, p. 2.) SoCalGas also states that it “fully supports TURN’s request to have its intervenor compensation for work involved with review of SoCalGas’ interstate capacity commitments to be considered in this proceeding.” (*Ibid.*)

Discussion

The GCIM is the structure which replaced the Commission's reasonableness reviews of SoCalGas' gas purchases and gas storage activities on behalf of its core sales customers. The GCIM is designed to provide SoCalGas with a financial incentive for making efficient gas purchasing decisions.

SoCalGas' Year 10 application states that it was able to purchase gas at \$27,028,710 below the GCIM benchmark. The actual cost of all the purchases subject to the GCIM was \$1,865,659,816 and the benchmark cost was \$1,892,688,526. Pursuant to the GCIM revisions adopted in D.02-06-023, SoCalGas requests a shareholder award of \$2,364,577 for Year 10.

ORA conducted a review, audit, and evaluation of the Year 10 GCIM results, the results of which are contained in ORA's Monitoring and Evaluation Report for Year 10. ORA's analysis confirmed the Year 10 GCIM results as follows:

“(a) the GCIM resulted in total shared savings of \$27,028,710, to be shared between ratepayers and SoCalGas shareholders. The shared savings were based on the difference between the actual costs of \$1,865,659,815 and the GCIM benchmark market index cost of \$1,892,688,526; (b) the total savings were confirmed as follows: to ratepayers \$24,664,133; to shareholders of SoCalGas, \$2,364,577....” (ORA, Monitoring and Evaluation Report, p. 2-1.)

As identified in the January 12, 2005 scoping memo, three issues have been identified in this proceeding. The first issue is whether SoCalGas should be awarded the amount it is requesting in its Year 10 application. The second issue is if the GCIM is modified or eliminated in I.02-11-040, how SoCalGas' GCIM award request for Year 10 will be affected. The third issue is whether TURN should be permitted to claim intervenor compensation in the GCIM for its work related to the consultation process for the interstate capacity commitment.

With regard to the first issue, SCE, ORA, and TURN do not dispute the calculation of SoCalGas' request for a shareholder award of \$2,364,577 for Year 10. Although SCE has raised concerns about the GCIM structure, SCE does not challenge the manner in which the shareholder award for SoCalGas was calculated. ORA's Monitoring and Evaluation Report verified that the amount and calculation of the shareholder award amount that SoCalGas is requesting for Year 10 is correct.

The second issue about whether the GCIM will be modified or eliminated in I.02-11-040, and its effect on the Year 10 shareholder award, has been previously addressed by us in the context of the shareholder awards for Years Seven, Eight, and Nine. In the three decisions addressing those three applications, we made each year's shareholder award subject to refund or adjustment. (*See* D.03-08-065, D.03-08-064, D.04-02-060.) No one opposes using the same approach for the Year 10 shareholder award.

The third issue identified in the scoping memo is whether TURN should be permitted to file for intervenor compensation in connection with the consultation process for interstate capacity. The scoping memo allowed TURN to file a notice of intent to claim compensation in this proceeding for work related to the consultation process.² Since TURN's notice of intent will be addressed in a future ruling in this proceeding, today's decision does not address the issue of TURN's request for compensation in connection with the consultation process for interstate capacity.

² Footnote 3 of the scoping memo noted that TURN also filed a request for compensation in R.04-01-025. Part of that request for compensation involves some work that is related to the consultation process.

After reviewing SoCalGas' application, the protests and responses to the application, and ORA's Monitoring and Evaluation Report for Year 10, we find that SoCalGas reasonably managed its gas acquisitions and operations in Year 10 within the context of the GCIM that existed at the time. However, since there is an ongoing investigation into what caused the high gas border prices from March 2000 through May 2001, today's finding does not prejudge what we may find or conclude in I.02-11-040 regarding the GCIM.

We also find that the calculation and amount of SoCalGas' shareholder award for Year 10 is correct. In accordance with the GCIM modifications adopted in D.02-06-023, SoCalGas is entitled to a shareholder award of \$2,364,577 for Year 10 of the GCIM. However, due to the ongoing activities in I.02-11-040, we may adjust the shareholder award for Year 10 if we decide in I.02-11-040 that the GCIM that SoCalGas operated under during Year 10 should be modified or eliminated. Thus, we will award SoCalGas a shareholder award of \$2,364,577 for Year 10 of its GCIM, subject to refund or adjustment, as may be determined in I.02-11-040. SoCalGas is permitted to adjust the Purchased Gas Account to reflect this shareholder award that may be subject to refund or adjustment.

Comments on Draft Decision

The draft decision of the Administrative Law Judge (ALJ) in this matter was mailed to the parties in accordance with Pub. Util. Code § 311(g)(1) and Rule 77.7 of the Rules of Practice and Procedure. No one filed comments on the draft decision.

Categorization and Need for Hearings

In Resolution ALJ 176-3136 dated July 8, 2004, the Commission preliminarily categorized this application as ratesetting, and preliminarily determined that hearings were not necessary. No protests have been received.

Given this status, a public hearing is not necessary and the preliminary determination made in Resolution ALJ 176-3136 does not need to be changed.

Assignment of Proceeding

Susan P. Kennedy is the Assigned Commissioner, and John S. Wong is the assigned Administrative Law Judge in this proceeding.

Findings of Fact

1. The GCIM provides an incentive for SoCalGas to purchase gas at or below the benchmark, and savings below the tolerance band are shared with ratepayers and SoCalGas' shareholders according to the sharing band.
2. The GCIM was modified in D.02-06-023, and SoCalGas was authorized to continue the use of the GCIM on an annual basis until modified or terminated by the Commission.
3. The January 12, 2005 scoping memo determined that no evidentiary hearings were needed, but a hearing may be needed in the future depending on the outcome in I.02-11-040 and if the Commission decides to modify or eliminate the GCIM.
4. SoCalGas acquired gas at a savings of \$27,028,710 below the GCIM benchmark in Year 10.
5. Although SCE has previously raised concerns about the GCIM structure, SCE does not challenge the manner in which the shareholder award for SoCalGas was calculated.
6. ORA's Monitoring and Evaluation Report for Year 10 verified the amount and calculation of the shareholder award.
7. No one opposes using the same approach that was used in the applications for Years Seven, Eight and Nine to resolve the issue about whether the GCIM

will be modified or eliminated in I.02-11-040 and how that may affect the Year 10 shareholder award.

8. Since TURN's notice of intent will be addressed in a future ruling, today's decision does not address the issue of TURN's request for compensation in connection with the consultation process for interstate capacity.

9. SoCalGas reasonably managed its gas acquisitions and operations in Year 10 within the context of the GCIM that existed at the time.

10. The calculation and amount of SoCalGas' shareholder award for Year 10 are correct.

Conclusions of Law

1. Today's finding regarding the reasonableness of SoCalGas' management of its gas acquisitions and operations in Year 10 shall not prejudice what the Commission may find or conclude in I.02-11-040.

2. No protests have been filed.

3. No hearing is necessary.

4. In accordance with the GCIM modifications adopted in D.02-06-023, SoCalGas is entitled to a shareholder award of \$2,364,577 for Year 10 of the GCIM.

5. Due to the ongoing activities in I.02-11-040, the Commission may adjust the shareholder award for Year 10 if the Commission decides in that investigation that the GCIM that SoCalGas operated under during Year 10 should be modified or eliminated.

6. SoCalGas should be awarded a shareholder award of \$2,364,577 for Year 10 of its GCIM, subject however to refund or adjustment, as may be determined in I.02-11-040.

7. SoCalGas should be permitted to adjust the Purchased Gas Account to reflect the shareholder award of \$2,364,577 that may be subject to refund or adjustment.

O R D E R

IT IS ORDERED that:

1. Southern California Gas Company (SoCalGas) is authorized to adjust the Purchased Gas Account to recognize a shareholder award of \$2,364,577 under Year 10 of its Gas Cost Incentive Mechanism.

2. SoCalGas's shareholder award amount of \$2,364,577 shall be subject to refund or adjustment as may be determined by the Commission in Order Instituting Investigation 02-11-040.

3. This proceeding shall remain open to address The Utility Reform Network's notice of intent to claim compensation in this proceeding.

This order is effective today.

Dated _____, at San Francisco, California.